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February 7, 2003



Mr. William F. Stephens
Virginia State Corporation Commission
Division of Energy Regulation
1300 E. Main Street – Tyler Building
P.O. Box 1197
Richmond, VA 23218-1197

RE: Case No. PUE- 2002-00645 - In the matter concerning the provision of
default service to retail customers under the provisions of the Virginia
Electric Utility Restructuring Act

Dear Mr. Stephens:

Delmarva Power & Light Company, d/b/a Conectiv Power Delivery, respectfully
submits its comments on the Commission's list of questions in the above-referenced
matter. We are sorry for the delay in getting Company's comments to you; however due
to the inclement weather experienced on Friday, February 7, 2003, Airborne Express had
cancelled their pickup service for our location.

If you should have questions, please contact me at 302-454-4830.

Sincerely,

A handwritten signature in cursive script that reads 'Gary Cohen'.

Gary Cohen
Special Projects Manager

GC/mar

cc: Service List
Guy Tripp, III, Esquire

S:/shared/mroy/cvrltr comment son default service-VA

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BEFORE THE STATE CORPORATE COMMISSION OF VIRGINIA

In the matter concerning the provision of default
service to retail customers under the provisions of the
Virginia Electric Utility Restructuring Act

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Case No. PUE- 2002-00645

DELMARVA POWER & LIGHT COMPANY
COMMENTS ON THE COMMISSION'S LIST OF QUESTIONS

On December 23, 2002 the Commission issued an order initiating this proceeding for purposes of investigating the provision of default service to retail customers under the provisions of the Virginia Electric Utility Restructuring Act ("Act"). In its order, the Commission posed thirteen specific questions for input and recommendations regarding the components of default service and the establishment of programs making such services available to retail customers. Delmarva Power & Light Company d/b/a Conectiv Power Delivery ("Delmarva" or "CPD"), now a subsidiary of Pepco Holdings, Inc., hereby submits comments on a list of questions contained in the December 23, 2002 order. Delmarva appreciates this opportunity to provide you with our views regarding the provision of default service to retail customers. Delmarva's views on this subject are to a large degree the product of the experience that it and its affiliates have had within the PJM region. This experience includes:

- o Delmarva currently performs the equivalent of what is referred to in Virginia as "default service" in Delaware and Maryland, where it is known by the name of "Standard Offer Service." At the present time, Delmarva's full requirements for this service is provided by an affiliate, Conectiv Energy Supply, Inc. ("CESI"), under a contract that places all risks and rewards with CESI. That is, Delmarva pays CESI an amount equal to the supply "shopping credit" in its unbundled Delaware and Maryland retail rates. CESI assumes the price and volume risks associated with default service, including costs associated with PJM's locational marginal pricing and congestion pricing mechanisms. There are rules in place in both Delaware and Maryland that reduce the risks related to larger customers who swing off and on the default service, i.e., either minimum stay requirements are imposed on a customer who returns to a fixed price default service or the price is variable based on PJM hourly energy rates and short-term capacity charges.¹
- o Delmarva affiliate Atlantic City Electric Company ("ACE") provides the equivalent of default service in New Jersey, where it is known as Basic Generation Service ("BGS"). At the present time, ACE's full requirements for this service are supplied through a wholesale bidding process that was established and bid-out by the New Jersey Board of Public Utilities (NJBPU) after months of negotiations and development by interested parties.
- o Delmarva affiliate Potomac Electric Power Company ("Pepco") provides the equivalent of default service in Washington D.C. and portions of Maryland. At the present time, Pepco's full

¹ Neither the minimum stay nor the variable price requirements are imposed currently on residential or the smaller C&I customers, but a 12-month stay-put requirement will begin for Delaware residential and smaller C&I customers beginning at the end of the current transition periods (Nov. 2003 and Nov. 2002, respectively).

requirements for this service are supplied under contracts with Mirant Corporation, which were entered into as part of a larger transaction involving the sale of the majority of Pepco's generating assets.

o Until approximately mid-2001, Delmarva affiliate Conectiv Energy Supply, Inc. ("CESI") had an active electric retail marketing business operating in Delaware, New Jersey, Pennsylvania, and Maryland. CESI and related companies not subject to utility rate regulation are currently in the business of generating and trading electric energy, primarily in the PJM region but also in other regions.

o Delmarva has recently become affiliated with Pepco Energy Services, Inc., which is an active electric retail marketer operating within Virginia, Delaware, New Jersey, Pennsylvania, Maryland, and the District of Columbia and also makes wholesale energy trades.

Delmarva's views with respect to the specific questions are as follows.

Question 1: What should be the specific components of default service.

Delmarva recommends that default service be limited to the provision of generation supply service. Delmarva believes a practical approach at this time would be to limit default service to the provision of generation supply service, and then assign a single entity to provide the entire default service obligation. For reasons set forth below, Delmarva also recommends that the incumbent electric utility supply the entire default service.

Delmarva also recommends that the default service provider satisfy its obligation through a competitive bid for full requirements products from the wholesale market. In order to assure cost recovery, special pricing rules would need to be established, which in Delmarva's situation, as a member of PJM, would include mechanisms that would allow for the recovery of PJM hourly locational marginal pricing for energy, the actual costs of capacity and/or capacity deficiency charges, PJM transmission and ancillary charges and other administrative costs associated with responding to an emergency.

In addition, if the incumbent utility is not the supplier of default service, processes would need to be established to deal with a default on the obligations by the third party default service provider. Such processes would establish mechanisms under which a third-party who has specifically contracted to be the emergency supplier would supply load and be compensated for whatever costs are incurred. Such emergency situations should be of short duration. Not only should the Commission establish regulatory mechanisms that would minimize the risks of a default by a competitive supplier of default services, but such mechanisms should also permit a rapid reassignment of the default service obligation to another willing provider in the event of a default by the original default service provider.

Question 2: Whether, given the virtual absence of competition in Virginia's retail generation market, incumbent electric utilities should continue to provide default service at capped rates at the present time; if so, what changes in statute, policy, infrastructure, market conditions, and/or other circumstances are necessary to allow for the practical provision of default service by an entity other than the incumbent?

Delmarva recommends that the incumbent electric utilities are the most appropriate providers of default service at this time. The rates for this service must, for legal and policy reasons, be based on the market prices paid for the supply procured in the competitive market. Default service should be a "safety-net" service to assure that generation service is available to all customers and all customer classes, including those customers that are unable to contract with or have been refused service by alternate generation suppliers.

For reasons described below, Delmarva questions whether it is realistic to have an unregulated or lightly regulated competitive bidder provide default service. Therefore, in responding to this question,

Delmarva also discusses briefly the concept of a competitive wholesale supply source that would be used by the incumbent in its provision of default service.

Retail Service

The experience of Delmarva and its affiliated utilities and non-utilities strongly suggests that customers, particularly smaller customers, will want and demand that the default service be a regulated service provided by an entity that they trust and with prices that are subject to a degree of stability. Moreover, many customers would view a switch to a third party default service provider without their consent as government "slamming." Testimony and filed comments in cases in both Delaware and Maryland have made clear that it is not just residential customers who value a utility service with some price stability. Commercial and most industrial customers also place a high value on price stability so that they can make future budget plans. It has also become clear through discussions with these customers that recent market conditions and the financial failure or distress of prominent energy companies have raised substantial concerns about having a non-utility supply the default service. While some such customers are willing to contemplate having a non-utility supply the component of default service involving customers who fail to choose a competitive supplier, there have been clear statements that customers also would seek a utility backstop even behind the competitive default service provider to deal with situations where the non-incumbent provider itself defaults on its obligations or declares bankruptcy.

Delmarva is opposed to making a non-incumbent responsible for only that portion of default service that involves customers who fail to choose a competitive retail supplier or are unable to find a willing competitive retail supplier for whatever reason. Delmarva believes that there should be one default service provider who will have sufficient load to plan a supply portfolio and assume the risk of non-paying customers. In Delmarva's view, it would be inordinately expensive for it or any other entity to act as a secondary backstop to the default supplier, either to provide service only to non-paying customers or stepping in on an emergency basis for a supplier who defaults on its obligations.

Question 3: What should be the geographic scope of a default service provider's territory, i.e. statewide, incumbent utility service territory, regions served by specific transmission entities; divisions with an incumbent utility's service territory; major metropolitan and surrounding areas, etc.

Due to differences among utility service territories, each utility service territory should have a default service provider providing service under rules, terms and conditions that take into account the specific attributes of the service territory. This is not meant to imply, however, that a default service provider operating within a single service territory should be precluded from participating in other service territories either as a competitive retailer or as a default service provider.

Question 4: Whether default service, as contemplated by § 56-585 of the Act, should be limited to unregulated services, i.e. is it necessary to designate distribution service as a default service?

Default service as contemplated by § 56-585 of the Act should be limited at this time to the unregulated service of generation. The Act gives clear guidance on this, as provided for in § 56-577 A 3: "On and after January 1, 2002, the generation of electric energy shall no longer be subject to regulation under this title, except as specified in this chapter." In addition, § 56-580 A provides: "The Commission shall continue to regulate pursuant to this title the distribution of retail electric energy to retail customers in the Commonwealth and, to the extent not prohibited by federal law, the transmission of electric energy in the Commonwealth."

Most notably, § 56-580 E of the Act specifically provides for the incumbent electric utilities to retain their rights to serve within their service territories: "Nothing in this section shall impair the distribution service territorial rights of incumbent electric utilities, and incumbent electric utilities shall continue to provide distribution services within their exclusive service territories as established by the Commission."

Issues relating to whether and when billing, meter reading and other similar services should be considered a "default service" should be deferred for consideration at a later time after the generation market has matured sufficiently.

Question 5: For generation-related default service, whether the separate components of generation service to retail customers (capacity or resource reservation, energy, transmission, and ancillary services) should be treated as separate default services or bundled into a single service.

At the retail level, these components should be bundled into a single service. PJM and the FERC, in fact, would require any "Load Serving Entity" operating within Delmarva's Virginia service territory to provide capacity, energy, transmission and ancillary services. At a wholesale level, however, these services may be acquired or self-supplied separately.

Question 6: For generation-related default service, whether the service should be delivered to the retail customer or to the incumbent utility.

Delmarva believes that at this time the existing infrastructure of the incumbent electric utility best supports the required customer care functions at the retail level and provides the best value to default service customers. The Company does not support a retail bidding model under which an alternative supplier would directly deliver default service to the retail customer.

While the term, "Supplier," by definition of the statute (Sec. 56-576) calls for the inclusion of selling "electric energy to retail customers," it is evident in other provisions of the VA Restructuring Act that the rights to provide retail service to customers is retained by the distributor or incumbent electric utility for its designated service area. Specifically, Section 56-580E of the Act states:

"Nothing in this section shall impair the distribution service territorial rights of incumbent electric utilities, and incumbent electric utilities shall continue to provide distribution services within their exclusive service territories as established by the Commission."

Delmarva believes that the most appropriate provider of default service at this time is the incumbent electric utility.

Question 7: Whether the language of the statute prohibits the provision of default service to an incumbent utility on behalf of a group of customers, i.e. could a third party provide service to an incumbent utility for indirect service to retail customers (service to satisfy load growth, specific localities, or to customer subgroups).

There is no statute in the Restructuring Act that Delmarva believes is specific to the form of aggregation discussed in this question.

Question 8: Whether the provision of default services should differ by customer class.

Delmarva believes that the Restructuring Act provides eliminating default service on a customer class basis; therefore, we interpret that default service can differ by class. § 56-585 E provides: "On or before July 1, 2004, and annually thereafter, the Commission shall determine, after notice and opportunity for hearing, whether there is a sufficient degree of competition such that the elimination of default service for particular customers, particular classes of customers or particular geographic areas of the Commonwealth will not be contrary to the public interest." With respect to commercial and industrial customers, in no event should default service provide a mechanism for more sophisticated customer to exploit default service by arbitraging the market against the default service rate. "Anti-gaming" rules that limit the ability of such customers to swing back-and-forth between default service and competitive retail service is a way that has been employed by many Commissions to prevent such abuses.

Question 9: Whether different components of default service can be provided by different suppliers.

Delmarva recommends that the default service provider (which should be the incumbent electric utility) should be responsible for full service requirements.

Question 10: Whether default service has the same meaning for different classes of customers, i.e., those who do not affirmatively select a supplier, those who are unable to obtain service from an alternative supplier, or those who have contracted with an alternative supplier who fails to perform.

Delmarva's interpretation of default service for the different classes of customers identified as examples in this question is that the Restructuring Act provides for the same meaning of default service to be applied for each of these customers.

Question 11: How should charges for default service be collected.

The retail customer served under default service should be billed and collected by the incumbent electric utility at the present time. The default supply service should use the existing rate structure, billing format, and collection process.

Question 12: Whether metering, billing and collecting services should be deemed components of default service.

Delmarva does not consider the metering, billing and collection services to be components of default service. There are currently work groups that have or in the process of developing the rules for these services. The work groups have found these issues to be extremely complicated, with little or no supplier participation or interest. In addition, the utilities are required to continue to maintain these required functions; therefore, Delmarva recommends the Commission limit its consideration of default service to the provision of generation service.

Question 13: What implications would the alternative provision of default service have for the determination of wires charges?

§ 56-583 of the Act provides that a utility can through either capped rates or wires' charges recover for stranded costs that are just and reasonable. Delmarva, as part of its restructuring settlement, has agreed not to assess a wires' charge and consequently has no comments on this matter.

Delmarva is appreciative of the opportunity to provide its comments and recommendations on the matter of default service to retail customers under the provisions of the Virginia Electric Utility Restructuring Act. The Company further welcomes the opportunity to work with Commission Staff and other interested parties on additional development of the recommendations surrounding this important issue that would ultimately provide the best value to customers.